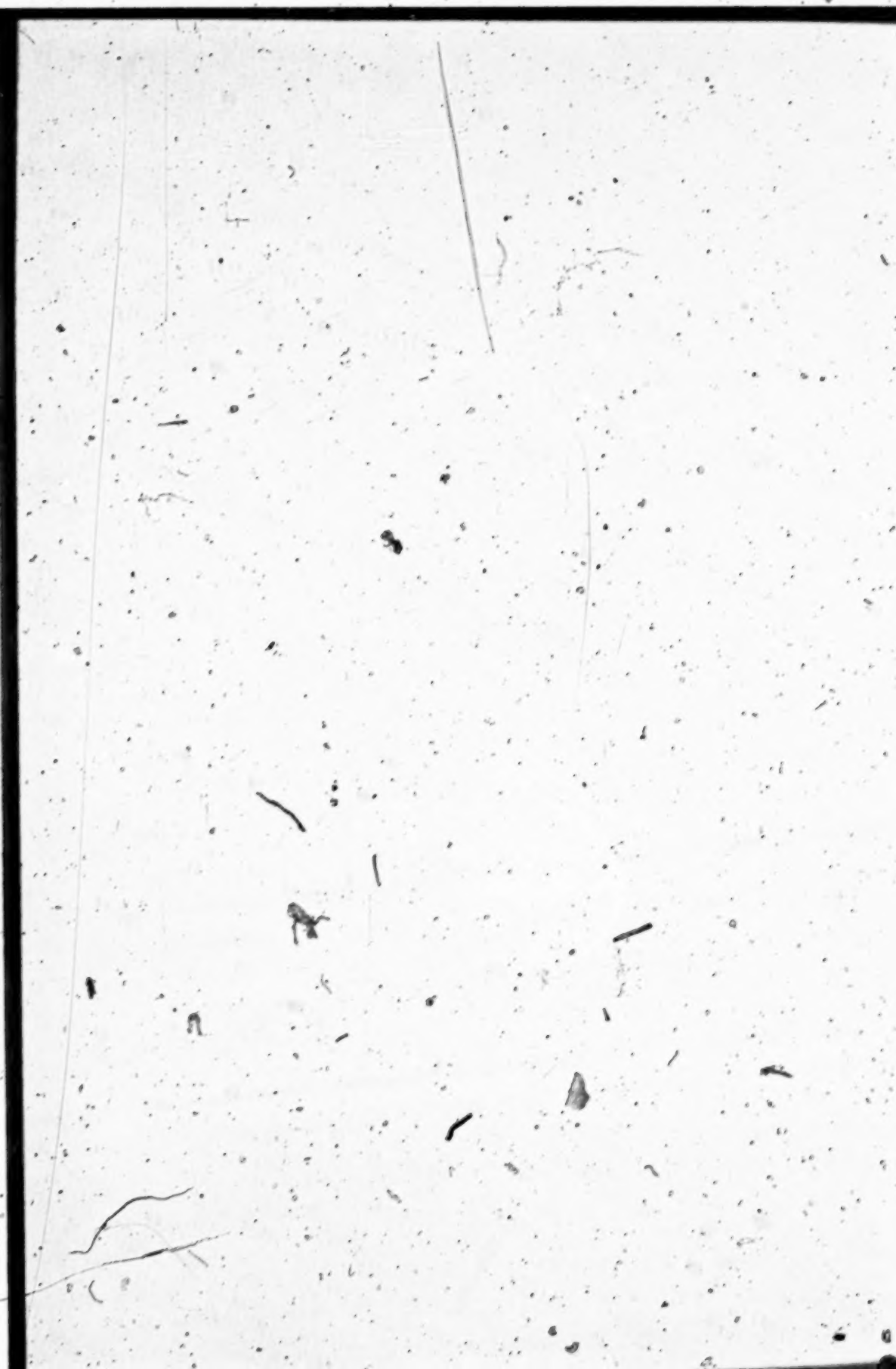

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1969

No. 921

THE CHASE MANHATTAN BANK, N.A., as Trustee under the General Income Mortgage of The New York, New Haven and Hartford Railroad Company,

Appellant,

v.

UNITED STATES OF AMERICA and INTERSTATE COMMERCE COMMISSION, *et al.*,

Appellees.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK

JURISDICTIONAL STATEMENT

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IN THE

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OCTOBER TERM, 1969

No. .....

THE CHASE MANHATTAN BANK, N.A., as Trustee under the General Income Mortgage of The New York, New Haven and Hartford Railroad Company,

Appellant,

v.

UNITED STATES OF AMERICA and INTERSTATE COMMERCE COMMISSION, *et al.*,

Appellees.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK

JURISDICTIONAL STATEMENT

Introduction

This jurisdictional statement is submitted on behalf of appellant, The Chase Manhattan Bank, N.A., as Indenture Trustee (Chase) under the General Income Mortgage of The New York, New Haven and Hartford Railroad Company (the New Haven). The General Income Mortgage secures $52,755,500 principal amount of Bonds, on which $7,121,994 of pre-bankruptcy interest is accrued and unpaid.*

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* These Bonds were issued in the 1947 reorganization of the New Haven under Section 77 of the Bankruptcy Act to holders of various defaulted debt securities of the New Haven system. The Bonds

Chase has appealed to this Court from the final decree of a majority of the three-Judge District Court for the Southern District of New York (the three-Judge Court) modifying slightly, and as so modified sustaining, the Fourth Supplemental Report and Order dated November 25, 1968 of the Interstate Commerce Commission (the Commission). The Commission's Fourth Supplemental Report and Order were issued in consolidated proceedings regarding the acquisition of the New Haven assets by Penn Central under Section 5(2) of the Interstate Commerce Act pursuant to Condition 8 of the Report and Order of the Commission permitting the merger of the Pennsylvania Railroad (Penn) and the New York Central Railroad (Central), and the appeal issues relate to the consideration payable by the merged Penn Central Company to the New Haven for assets of the New Haven under said Condition 8.

The merger of Penn and Central took place February 1, 1968, and Penn Central acquired the assets of the New Haven eleven months later, on December 31, 1968, pursuant to Orders (A-218a and A-269a) of the Commission and the District Court for Connecticut (the New Haven Reorganization Court under Section 77 of the Bankruptcy Act), each containing the proviso that it remained open for any party to contest the consideration to be paid by Penn Central to the New Haven, as determined in accord-

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were secured by a system mortgage running to an Indenture Trustee, The Chase National Bank of the City of New York, which in 1955 became The Chase Manhattan Bank, N.A. The Bonds are junior to, and therefore have a position different from, the system First and Refunding Mortgage Bonds. Accordingly, it has seemed inappropriate as well as impracticable for the Chase, as Trustee under the General Income Mortgage, to join in a jurisdictional statement on this appeal with representatives of the First and Refunding Mortgage interests.

ance with Condition 8, for the assets conveyed to Penn Central. Condition 8 provided that the merged Penn Central should take over assets of the New Haven at a fair and equitable price approved by the Commission and the Reorganization Court. Thus the Reorganization Court was to be a coequal arbiter with the Commission as to such price or consideration, as well as having to pass judgment on the price as part of the reorganization of the New Haven under Section 77 of the Bankruptcy Act.

The consideration, fixed by the Commission in its Fourth Supplemental Report as purporting to equal the value of the New Haven assets taken over and to total $140,600,000,* consisted principally of 950,000 shares of Penn Central stock (taken at $87.50 per share), some Penn Central 5% bonds, and a small amount of cash.

The Reorganization Court, the coequal arbiter under Condition 8, has rendered a decision disapproving as too low by at least $28,000,000, and possibly $98,000,000, the consideration fixed by the Commission and approved by two Judges of the three-Judge Court. One Judge of the three-Judge Court has also disapproved of such consideration as much too low.

Accordingly, two Judges, Friendly, Circuit Judge, and Levet, District Judge, have approved such consideration, and two Judges, Anderson, Circuit Judge (sitting by designation in the Reorganization Court), and Weinfeld, District Judge, have disapproved such consideration as far too low.

Consequently, there is a stalemate. The purchaser, Penn Central, and the seller, New Haven, are subject to con-

* Exclusive of $5,000,000 paid for only a portion of the losses of the New Haven from the date of the Penn Central merger to the date of the inclusion of the New Haven assets.

flicting decisions regarding the consideration payable for the New Haven assets. As will be shown, the issues presented are important and substantial.

In accordance with the statutes, in addition to the appeals directly to this Court from the three-Judge Court decision, appeals have been taken to the Court of Appeals for the Second Circuit from the decisions of the Reorganization Court relating to the Commission's Fourth Supplemental Report (and also the Second Supplemental Report), and petitions for writs of certiorari are being filed in this Court asking this Court to take up and hear those appeals directly simultaneously with the direct appeals to this Court.

As both Courts have stated, the dilemma presented by the conflicting views can only be resolved by this Court. The majority of the three-Judge Court said, "reconciliation of divergent views will come ultimately in the nation's highest court, which alone can speak with authority" (Opinion of June 18, 1969, A-431a),* and "The difference in the treatment of this item [a discount of $2,700,000, discussed in VI below] by the two courts will be another matter for ultimate resolution by the Supreme Court" (Opinion of September 11, 1969, A-445a). The Reorganization Court, referring to the conflict between the Commission's Report and its own determinations, said: "This price difference alone makes appeals and cross-appeals from both courts inevitable" (Supplemental Opinion, July 28, 1969, A-314a). The Reorganization Court then supported this conclusion by referring to (i) the dispute over non-payment by Penn Central for a major asset potentially worth $70,000,000 conveyed to it by the New Haven, and (ii) the price of $87.50 per share at-

* References to "A- " will be to pages of the separate Appendix.

tributed by the Commission to the 950,000 shares of Penn Central stock (as bolstered by the underwriting "formula" invented by the Reorganization Court) which is the major part of the consideration (A-314a and 315a).*

Appellant submits this statement to show that the Supreme Court of the United States has jurisdiction of this appeal and that substantial questions are presented.

Opinions Below

The majority and minority opinions of the three-Judge Court filed June 18, 1969 and the September 11, 1969 decree and memorandum by the majority relating to the Commission's Fourth Supplemental Report have not yet been reported.** The Commission's Fourth Supplemental Report and Order dated November 25, 1968 are reported at 334 I.C.C. 25.** The prior majority and minority opinions of the three-Judge Court on the same subject matter but directed to the Commission's Second Supplemental Report are reported at 289 F. Supp. 418.** The Second Supplemental Report of the Commission dated November 16, 1967 is reported at 331 I.C.C. 643.**

The opinion of the Reorganization Court filed May 28, 1969 and directed to the Fourth Supplemental Report is not yet reported.** The earlier opinion in this litigation of the Reorganization Court directed to the Second Supplemental Report is dated August 10, 1968 and is reported at 289 F. Supp. 451.**

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* The Penn Central stock was selling at about $63 per share at the time of the transfer of New Haven assets to Penn Central. It has sold as high as 71 during 1969 and has recently been selling at about $31 per share.

** Copy printed in separate Appendix.

There were only two Reports of the Commission which have been before the Courts relating to the consideration to be paid for the New Haven assets—the Second and Fourth Supplemental Reports. The First and Third Reports do not relate to that matter.

The Commission's Fifth Supplemental Report on reconsideration as modified August 26, 1969 was issued without notice to any party or any hearing and *after* both Courts had rendered their opinions and is reported at 334 I.C.C. 528.*

Jurisdiction

This suit was brought and maintained in the three-Judge Court pursuant to 28 U.S.C. §§ 1336, 2284 and 2321 to 2325, inclusive, to annul, set aside and enjoin the enforcement of, the Commission's Fourth Supplemental Report and Order made under Section 5(2) of the Interstate Commerce Act prescribing the consideration payable by Penn Central to the New Haven for its assets.

The decree sought to be reviewed is dated September 11, 1969 and was entered on that date. The Chase Notice of Appeal was filed on October 9, 1969 in the United States District Court for the Southern District of New York.

The jurisdiction of the Supreme Court over the appeal from the decree of the three-Judge Court is conferred by 28 U.S.C. § 1253. The following decisions sustain the jurisdiction of the Supreme Court to review said decree on direct appeal: *Penn-Central Merger Cases*, 389 U.S. 486 (1968); *B.&O. R. Co.* v. *United States*, 386 U.S. 372 (1967); *Seaboard Air Line R. Co.* v. *United States*, 382 U.S. 154 (1965).

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* Copy printed in separate Appendix.

Provisions of Constitution and Statutes Involved

The following are printed in the separate Appendix at A-453a *et seq.*:

The Fifth Amendment to the Constitution of the United States (A-453a).

Section 5(2) of the Interstate Commerce Act (49 U.S.C. § 5(2)) (A-453a).

Sections 1(18) and 1(20) of the Interstate Commerce Act (49 U.S.C. §§ 1(18) and 1(20)) (A-457a).

Provisions of Section 77(b), (d) and (e) of the Bankruptcy Act (11 U.S.C. § 205(b), (d) and (e)) (A-458a, 461a and 463a).

Questions Presented

1. Whether after the Commission, pursuant to Section 5(2) of the Interstate Commerce Act, had approved the application of Penn and Central to merge on condition that the merged company acquire the railroad operations and assets of the New Haven on fair and equitable terms as determined by the Commission and the Reorganization Court, the New Haven was entitled to receive as compensation from Penn Central the liquidation value of the assets transferred to Penn Central, which the New Haven could have realized on such assets if they had been condemned or if the New Haven had been liquidated? (Discussed in I below)

2. Whether, in the case of a deficit railroad such as the New Haven, the Commission could legally reject net liquidation value as the valuation standard and arbitrarily announce as fair and equitable a value and price for such

assets without having followed any legal standard of valuation? (Discussed in I below).

3. Whether the unanimous conclusion of the three-Judge Court in its July 1968 decision, concurred in by the Reorganization Court in its August 1968 decision, (a) that the price payable by Penn Central could not be less than liquidation value and (b) that § 1(18) of the Interstate Commerce Act calling for the Commission's consent to an abandonment could not stand in the way of a liquidation valuation as of December 31, 1966 because of the New Haven's constitutional right on the facts shown by the record to cease its railroad operations, was the law of the case which should not have been departed from in the Commission's Fourth Supplemental Report or in the opinion of two Judges of the three-Judge Court filed June 18, 1969? (Discussed in I below)

4. Whether, after the New Haven had been operated for over seven years in proceedings under Section 77 of the Bankruptcy Act with large and increasing operating losses and without any prospect of decreasing such losses or operating as a profitable railroad, the New Haven and its creditors would have the right to discontinue the losing railroad operations and realize the liquidation value of the New Haven assets pursuant to the Fifth Amendment of the Constitution of the United States prohibiting the taking of private property for public use without just compensation and prohibiting deprivation of property without due process of law? (Discussed in I below)

5. Whether Penn Central's present inability to realize by sale the net liquidation value of the New Haven assets sold to it because it is in the public interest that Penn Central continue the deficit New Haven operations, which

Penn Central had agreed to do as a condition of effecting the merger of Penn and Central, was a legal basis for the Commission's prescribing a price payable by Penn Central to the New Haven substantially below the net liquidation value which the New Haven could have realized for such assets? (Discussed in I below)

6. Whether, after the three-Judge Court and the Reorganization Court in the summer of 1968 determined (a) that the Commission's finding that about $125,000,000 of net proceeds would be realized in a liquidation by the New Haven of the assets here involved over a six-year liquidation period was erroneous because it was far below net liquidation value and (b) that net liquidation value was the minimum to which the New Haven was entitled, and after that Court had therefore remanded the proceeding to the Commission for a substantial increase of its rejected finding of liquidation value, the Commission acted arbitrarily, capriciously and without substantial support in the record by increasing its liquidation value finding only to $162,700,000 and by then reducing that liquidation value finding by conjuring up (i) an additional year's delay of the six-year liquidation period which would allegedly reduce the new finding of net liquidation value by $15,400,000 and (ii) a new so-called bulk sale discount of $6,700,000 which would further reduce such net liquidation value? (Discussed in II, III, V and VI below)

7. Whether, after the three-Judge Court in its July 1968 decision determined that the Commission's $125,000,000 finding of the liquidation value of the New Haven assets, based on a six-year liquidation period, might well be inadequate in the range of $45,000,000 to $50,000,000 (the Reorganization Court in its August 1968 decision finding the range of deficiency to be between $33,000,000 and

$55,000,000) and after both Courts remanded the respective proceedings to the Commission for further action in accordance with the opinions of the two Courts, which opinions in no way questioned the six-year liquidation period, the Commission lacked power largely to increase its finding of liquidation expenses by stretching out the liquidation period by an additional year and by adding a large new item of expense for the purpose of decreasing its new net liquidation value finding of $162,700,000 by $22,000,000? (Discussed in II(a) and (b) below)

8. Whether the price of approximately $141,600,000 payable by Penn Central for the New Haven assets prescribed by the Commission in its Fourth Supplemental Report as modified and approved by the majority of the three-Judge Court, which price was far less than the net liquidation value of such assets, was without substantial support in the record and was arbitrary and capricious? (Discussed in II, III, V and VI below)

9. Whether, after concluding that the New Haven had a 50% interest in those net earnings of the Grand Central Terminal hotels and office buildings which were in excess of the amount thereof used to defray Terminal expenses, the Commission acted arbitrarily and capriciously and without substantial support in the record in ruling that the New Haven's interest (about $5,600,000 annually) in those hotel and office building net earnings which had been used to defray Terminal expenses payable by the New Haven was to be transferred by the New Haven to Penn Central free and clear of any restriction without the New Haven's receiving any compensation therefor, although potentially worth some $70,000,000? (Discussed in III below)

10. Whether the Commission erred in arbitrarily limiting to $5,000,000 the amount which Penn Central should bear of the more than $10,000,000 of losses of the New Haven incurred by reason of the deferment for Penn Central's convenience and benefit of New Haven's inclusion in Penn Central from February 1, 1968 (when Penn and Central were merged) until December 31, 1968 (when the New Haven was included in the merged company)? (Discussed in IV below)

11. Whether the Commission erred in arbitrarily excluding certain items of loss from the formula determining the amount which Penn Central should bear of the New Haven losses for the 11-month period February 1, 1968 through December 31, 1968? (Discussed in IV below)

12. Whether the Commission was arbitrary and capricious and without substantial support in the record in accepting as the value of the New Haven's Harlem River and Oak Point Yards the $18,100,000 appraisal thereof which assumed cessation of railroad service to such Yards upon the New Haven's liquidation instead of the adjusted $22,540,000 appraisal thereof by the same appraiser which assumed that railroad service to those Yards would be continued? (Discussed in V below)

13. Whether the Commission's failure to reduce by at least $2,415,000 the $17,563,000 discount to present worth which the Commission deducted in its valuation of the New Haven assets being sold to Penn Central was arbitrary and capricious and without substantial support in the record? (Discussed in VI below)

14. Whether the formula invented by the Reorganization Court and adopted by the three-Judge Court to

guarantee the $87.50 value per share assigned by the Commission to the Penn Central stock received by the New Haven contains provisions which would interfere with the achievement of a basic intention of the reorganization plan? (Discussed in VII below)

Statement of the Case

The proceeding for reorganization of the New Haven under Section 77 of the Bankruptcy Act commenced on July 7, 1961 in the District Court for the District of Connecticut (the Reorganization Court) presided over by Judge Anderson, Chief Judge of the District Court. He continued to preside over the Reorganization Court when he became a Circuit Judge, thereafter sitting by designation.

In 1962, Penn and Central instituted a proceeding before the Interstate Commerce Commission under Section 5(2) of the Interstate Commerce Act for authority to merge. The New Haven Section 77 Trustees intervened in that proceeding asking that, as a condition of the merger, Penn and Central be required to give the New Haven the option of being included.

In its Report and Order dated April 6, 1966, the Commission authorized the merger of Penn and Central subject to the following Condition 8 relating to the inclusion of the New Haven (first paragraph) (327 I.C.C. at p. 553):

> "8. The Pennsylvania New York Central Transportation Company shall be required to include in the transaction all the New York, New Haven and Hartford Railroad Company—the inclusion of passenger operations being subject to the findings and determinations of the Commission as set forth in

> Finance Docket No. 23831 issued simultaneously with this report—upon such fair and equitable terms as the parties may agree subject to the approval of the Bankruptcy Court and the Commission. Within 6 months after the date this report is served, the parties shall file with the Commission for its approval, a plan for such inclusion. In the event the parties are unable to reach an agreement (and subject to approval by the Bankruptcy Court) such inclusion shall be upon such fair and equitable terms and conditions as the Commission may impose."

Thus, as previously stated, the Reorganization Court is made the coequal arbiter of the consideration along with the Commission. Condition 8 (third paragraph) further provides (327 I.C.C. at p. 553) that consummation of the merger by Penn and Central shall signify their full and complete consent to the requirements of Condition 8. This Court has ruled that Penn Central "will perforce accept" such conditions "by its act of merger" (*Penn-Central Merger Cases*, 389 U.S. at p. 510).

In October 1966, the New Haven's Trustees filed with the Reorganization Court and with the Commission "Step I" of a plan of reorganization proposing terms and conditions upon which assets of the New Haven would be acquired by Penn and Central in connection with their merger. Penn and Central joined in asking the Commission and the Court for approval of such terms and conditions. This incomplete plan of reorganization has been termed Step I in these proceedings since it envisaged that, after the sale of the New Haven to Penn Central and the determination of the consideration to be paid to the New Haven, the remainder of the plan of reorganization, namely, provisions concerning the capitalization of the reorganized New Haven and the allocation of its securities among its creditors,

would be proposed as "Step II". (This has been done, but Step II issues were not before the three-Judge Court and are not being presented to this Court.)

Penn and Central, after secret negotiations with the Section 77 Trustees of the New Haven who refused to inform the New Haven security holders of how they were proceeding, had entered into a tentative agreement in April 1966 with such Trustees for the purchase of the New Haven assets, which agreement was expressly subject to the approval of the Commission and the Reorganization Court and was further subject to effectuation of the Penn Central merger. The approval of the Reorganization Court was never obtained by the New Haven Trustees, nor was it requested until they made their Step I application which included such purchase agreement.

The Commission rendered its Second Supplemental Report and Order dated November 16, 1967, approving the consideration to be paid by Penn Central to the New Haven's Trustees substantially as provided in the above-mentioned agreement which had never been authorized by the Reorganization Court.

Believing the proposed consideration to be grossly inadequate, representatives of the New Haven's bondholders then commenced Court proceedings to review the Commission's Second Supplemental Report and Order in the three-Judge Court. The Report and Order were also certified to the Reorganization Court as part of a plan of reorganization under Section 77 of the Bankruptcy Act and hearings were held thereon. The two Courts recognized that they each had separate jurisdiction to review the Step I issues. The three-Judge Court had jurisdiction to review the Commission's decision on such issues because the decision was made under Section 5(2) of the Interstate Commerce Act,

while the Reorganization Court had jurisdiction under Section 77 of the Bankruptcy Act over all parts of a plan of reorganization as well as jurisdiction under the Commission's Condition 8 over the terms and conditions of the inclusion of the New Haven in Penn Central.

That there would be review both by the Reorganization Court and a statutory District Court was recognized by this Court's opinion in *Penn-Central Merger Cases,* 389 U.S. 486 (Jan. 15, 1968) at pp. 507-511. There this Court (at p. 507 *et seq.*) briefly describes some of the history of the New Haven proceeding and at p. 509 notes that the inclusion terms in the Commission's Second Supplemental Report had "not been reviewed by the bankruptcy court or by a statutory district court under the applicable statute." This Court ruled (p. 511) that such review could take place after consummation of the Penn Central merger. The Penn Central merger was effected February 1, 1968. The New Haven was included eleven months later, December 31, 1968.

Both Courts below held that the proposed Step I price approved in the Commission's Second Supplemental Report was inadequate by many millions of dollars ($45,000,000 to $50,000,000, 289 F. Supp. at p. 440, as decided by the three-Judge Court in July 1968 (A-358a); and $33,000,000 to $55,000,000, 289 F. Supp. at p. 465, as decided by the Reorganization Court in August 1968 (A-256a)). Therefore, both Courts at that time remanded the proceedings to the Commission.

The Commission thereafter issued its Fourth Supplemental Report and Order dated November 25, 1968 (334 I.C.C. 25, A-112a *et seq.*), increasing the price payable by Penn Central by some $15,000,000 which was far less than had been indicated in the remand decisions of the two Courts.

In the Fourth Supplemental Report and Order, the Commission, subject to the approval of the Reorganization Court, directed Penn Central to take over the New Haven at the end of 1968 upon payment of the consideration which had been approved by the Commission (but not by the Reorganization Court), without prejudice to further litigation as to the price and terms of the inclusion (A-219a, A-163a). The Reorganization Court approved the take-over by an order dated December 24, 1968 (A-269a), also without prejudice as to contesting the consideration (A-275a).

The three-Judge Court (one Judge dissenting) and the Reorganization Court thereafter rendered decisions as to the amount and value of the consideration specified in the Commission's Fourth Supplemental Report which, as stated, conflicted in important respects discussed herein.

The Questions Presented are Substantial

The ensuing discussion of the questions presented will show that they involve issues which are substantial and important and some of which require adjudication by this Court to resolve the stalemate caused by dual review of the same issues in different Courts in proceedings under two different statutes, the Interstate Commerce Act and Section 77 of the Bankruptcy Act.*

* Several appellees have indicated that in their responses they may propose to the other parties to these appeals an expedited procedure which, subject to this Court's approval, would include an abbreviated briefing schedule. For this reason, the discussion in this jurisdictional statement of the questions in controversy is somewhat longer than it would otherwise be.

(I) Erroneous repudiation by majority of the three-Judge Court of that Court's earlier ruling and the ruling of the Reorganization Court that net liquidation value was the appropriate legal standard of valuation in this case.

(Questions 1, 2, 3, 4 and 5)

In holding that the Commission was free in its valuation process to refuse to follow any legal standard of value and could pluck a valuation figure from the air so long as the Commission said it was fair and equitable, the June 18, 1969 majority Opinion of the three-Judge Court (A-404a to 411a) is in conflict not only with the minority of the three-Judge Court (minority Opinion June 18, 1969, A-434a) and with the Reorganization Court (Opinion of May 28, 1969, A-281a), but also is in conflict with its own prior July 10, 1968 Opinion (289 F. Supp. at pp. 440-1, A-359a to 361a).*

Thus, the three-Judge Court in that first decision (289 F. Supp. at pp. 440-1, A-359a to 361a) ruled unanimously that "the proper legal standard" in this case was liquidation value and that "the price cannot be less than the liquidation value".

Yet, the majority of the three-Judge Court (in the June 18, 1969 majority Opinion, A-406a to 411a) evades that threshold issue and holds in effect that the Commission need follow no legal valuation standard (majority June 18, 1969 Opinion, A-410a and 411a).

The reasoning advanced for departing from the liquidation value standard was that of the Commission, which asserted that Penn Central would be required to continue the New Haven's deficit operations and, since it therefore

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* The holding also conflicts with prior holdings of the Commission itself, *e.g., New York Central Acquisition of Chicago, Attica & S.R. Co.*, 187 I.C.C. 527 (1932) where the Commission said (p. 549): "Proof in this instance that the owners of the Attica can realize a substantial sum by scrapping the property fixes the commercial value at not less than that amount."

could not realize net liquidation value of the New Haven assets, the New Haven should not be allowed to do so either (334 I.C.C. at pp. 66, 75, A-153a and 162a). The Commission also raised the issue whether it had to follow any legal standard in fixing a price for the New Haven assets, claiming that it did not have to do so (334 I.C.C. at p. 53 *et seq.*, A-140a *et seq.*).

The Commission argued that the public interest or need prevented the New Haven's being shut down and its assets liquidated. It said that the Commission has imposed on Penn Central the requirement of absorbing the New Haven, "which requirement rests entirely upon the public's need for a continuing NH" (334 I.C.C. at p. 54, A-141a). The Commission also said that, in view of its finding that there was a public need for the railroad, the creditors may not liquidate the New Haven or devote the properties to another use (334 I.C.C. at p. 55, A-142a). Again, the Commission said (334 I.C.C. at p. 61, A-148a) "Even if not necessary in the private interest, where there is no longer a going concern value to preserve, the public need for the rail service may require its preservation as a going concern."

Accordingly, Penn Central was the instrumentality chosen by a public authority (the Commission) to continue the operation of the railroad in the public interest and to block New Haven's right to liquidate and thereby to obtain liquidation value. This is no less than a condemnation by means of Penn Central.

The Special Master (John Van Voorhis, until recently a New York Court of Appeals Judge) recognized that there was here involved a transaction in the nature of a condemnation of the New Haven. He said (June 17, 1968 Report, p. 45):

> "in a number of respects, it is analogous thereto," and further: "this amounts in reality (whether or not it

does in name) to a taking of the property of the bondholders without their consent. This is not a proceeding in the Court of Claims but the Constitution binds the Reorganization Court as well and that means that private property cannot be taken for a public use (railroads are affected with a public interest and empowered to condemn for that reason) without payment of just compensation."

A decision of this Court in which the New York Central Railroad Company and the New York and Harlem Railroad Company were defendants as condemnors strongly supports this view, *Muhlker* v. *New York and Harlem Railroad Company, et al.*, 197 U.S. 544 (1905).

In that case these railroad companies had been directed by a New York statute to construct an elevated railroad structure over Park Avenue and to lift their tracks from the street and to put them on the elevated structure. The plaintiff was the owner of property abutting on the Park Avenue structure and he claimed that the railroad companies in complying with the statute became liable to him for condemning his property by way of impairing his easements of light and air. As in the present case, the condemning railroads argued that the plaintiff's easements were subject to the police power and the taking was required by the State in the public interest and that they were not liable for the taking. The Supreme Court held that the railroads were in fact condemning the plaintiff's easements pursuant to authority and direction of the State and were liable for the damages.

Here, as the Commission says, by reason of the requirement imposed by the Commission in order to block liquidation, Penn Central is taking the property of the New Haven to keep it operating because of the public interest. Consequently, since liquidation is prevented by such taking of

Penn Central for the public interest, Penn Central is liable for the property taken in the amount of the liquidation value of the property. If the New Haven and its bondholders do not receive at least liquidation value, it will constitute a violation of the due process clause and a taking of private property for public use without just compensation—all contrary to the Fifth Amendment to the Constitution of the United States.

This principle was fully recognized by the three-Judge Court in its first decision (289 F. Supp. at pp. 440-1, A-359a to 361a).* The Reorganization Court came to the same conclusion, but without even needing to reach the constitutional ground (289 F. Supp. at p. 454, A-239a).

As stated above, the Commission has argued that the inclusion of the New Haven is a burden to Penn Central and not valuable to Penn Central, for one reason because Penn Central cannot realize the liquidation value (334 I.C.C. at p. 66, A-153a). But it has been authoritatively held that, in the case of a taking either by a public authority such as a city, or by an instrumentality on behalf of a public authority in the public interest, the fact that the property taken has lesser value to the taker than it has to the owner, or even has no value to the taker, does not relieve the taker from paying to the owner the full value of the property taken (*Matter of City of N. Y. (Fifth Avenue Coach Lines, Inc.)*, 22 N.Y.2d 613 (1968)).

There the New York Court of Appeals confirmed its prior decision in *Matter of Port Auth. Trans-Hudson Corp.* [*Hudson Rapid Tubes Corp.*], 20 N.Y.2d 457 (1967), *cert.*

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* The three-Judge Court said (289 F. Supp. at p. 441, A-360a and 361a) that "when the asking price for the acquired road is what the Constitution demands the owners must receive as a condition to allowing the road to be operated in the public service, we think—subject only to what we shall say hereafter as to interim losses—that the Commission may not fix, or approve, anything less".

denied 390 U.S. 1002 (1968), by holding that the City which had taken the properties of the Fifth Avenue Coach Company must pay to it the value of its franchises although the franchises were of no value to the City because they were not needed by the City to operate the bus lines.

In the *Port Authority* case, *supra*, the condemned railroad facility was found to be inherently incapable of operating at a profit and its liquidation value was also found to be nominal but the Court of Appeals fixed the condemnation price at depreciated original cost which was many millions of dollars above the nominal liquidation value.*

The fact that Penn Central is obligated to continue the deficit New Haven operations and, therefore, cannot realize net liquidation value is also erroneously referred to by the majority of the three-Judge Court in its June 18, 1969 Opinion (A-407a) as a possible basis for depriving the New Haven even of net liquidation value. That the New Haven would be entitled to discontinue operations and liquidate after years of mounting losses has been recognized by all the Judges of both Courts below.** It is clear that the public interest in continuance of New Haven deficit operations could not constitutionally deprive the New Haven of that right to discontinue and of the accompanying right to real-

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* The Court of Appeals said (20 N.Y. 2d at p. 468):

"We are here concerned with a property which has a usefulness created by the owner himself through the expenditure of large sums of money and by the continued operation of the property for the very purpose for which the petitioner is acquiring the property. It is the owner who built the 'reservoir'—the Tube railway system in the present case. This owner has developed its property at a cost of millions of dollars and operated it for more than 50 years. It is admittedly of great usefulness in the daily transportation of thousands of commuters. A condemnor should not be permitted to tell him: 'It's only worth scrap or less'."

** For example, the three-Judge Court in its initial opinion said unanimously with respect to a Penn Central contention (289 F. Supp. at p. 440, A-359a) that "this ignores the constitutional right of NH to cease operation and liquidate".

ize net liquidation value. The Commission, in its first decision (Second Supplemental Report) determining the consideration, did not make any deduction from liquidation value on account of any obligation of Penn Central to continue a losing railroad operation on the New Haven.

As the Reorganization Court said in its May 28, 1969 Opinion (A-291a):

> "Its [the Commission's] declared reasons for not doing so [not giving the New Haven liquidation value] are transparent pretexts under the cover of which the Commission arbitrarily and capriciously confers a benefit—not on the public—but on Penn Central, which would obtain New Haven's assets at a price substantially below fair liquidation value and yet comply with the condition for the Pennsylvania-New York Central merger that it take over the New Haven."

Penn Central is in no position to complain of the fact that the public interest requires Penn Central to acquire the New Haven assets and use them to continue the New Haven deficit operations, since Penn Central agreed to do just that as the price of being authorized to effect its merger.

So far as the argument advanced by the Commission that it need use no standard of valuation is concerned, the Reorganization Court correctly said in reference to the initial review decisions (Opinion of May 28, 1969, A-281a):

> "Both reviewing courts decided that under the circumstances of this case the only feasible standard for determining price must, because of both the 'fair and equitable' clauses of the statutes and the constitutional mandate, be the fair liquidation value, which is the property's highest and best use."

Such unanimous holding on the initial review that liquidation value was the proper valuation standard here should

have been adhered to thereafter by the three-Judge Court as the "law of the case". The Reorganization Court expressly so held (May 28, 1969 Opinion, A-286a). The thrust of the June 18, 1969 opinion of the minority of the three-Judge Court is to the same effect. Indeed, the dissenting Judge takes the position (A-434a *et seq.*) that the majority in the opinion of the same date adheres to the liquidation value standard and that the error of the majority lies in making unjustified deductions from liquidation value.

(II) The two new discounts conjured up by the Commission are specious and unwarranted, as the Reorganization Court and the dissenting Judge of the three-Judge Court found.

(Questions 6, 7 and 8)

The Commission sought in its Fourth Supplemental Report to reduce the price to an amount substantially less than net liquidation value (specifically found by it to be $162,700,000) by deducting $22,000,000 of what it called "other pricing considerations", but which really were newly concocted additional liquidation expenses. The invitation to the Commission in the July 10, 1968 three-Judge Court decision (289 F. Supp. at p. 441, A-361a) was not to propose new items of expense, but was only to submit an alternative legal standard (another "pricing theory") for consideration by the Supreme Court if the Commission disagreed with the net liquidation value standard approved in that three-Judge Court decision and in the concurring opinion of the Reorganization Court.

For the Commission to deduct millions of dollars of additional expenses from the specific new finding of net liquidation value was not a proposal of an alternative standard of value. The Commission was not warranted on remand to make such reductions from net liquidation value on pretexts which the Commission had never theretofore

suggested. The Reorganization Court said in its Opinion of May 28, 1969 (A-291a): "The Commission never entertained any such concept on the first round". As the dissenting Judge of the three-Judge Court said in his recent opinion (A-433a), the Commission "gave with one hand and took away with the other".

We discuss in subpoints (a) and (b) below the two new unwarranted discounts.

(a) *Unjustified "stretch out" of six-year liquidation period so as to decrease the net liquidation value and price by $15,386,000.* By far the larger of the Commission's two new discounts purports to be based on a "stretch out" of the six-year period of liquidation used in both the Second Supplemental Report and the Fourth Supplemental Report in arriving at net liquidation value. This one-year "stretch out" was estimated by the Commission to require a reduction of $15,386,000 from net liquidation value in order to arrive at a purchase price. Such deduction was in addition to the enormous expenses which had already been deducted in arriving at a net liquidation value figure on the basis of an assumed six-year period of liquidation commencing December 31, 1966. The "stretch out" was based on the supposition that, in addition to the six-year period of liquidation, there would be a further delay of one year to obtain a certificate from the Commission permitting cessation of New Haven's operations.

The three-Judge Court in its first decision expressly overruled the Penn Central contention of additional delay for an abandonment proceeding by saying unanimously (289 F. Supp. at pp. 438-9, A-354a and 355a):

> "A much more significant item is raised by the claim that before the NH Trustees could even begin a liquidation, lengthy abandonment proceedings would be re-

quired, during which large cash losses would be incurred and the property would further depreciate. The bondholders respond that if inclusion of NH in Penn Central had not been in prospect, the NH Trustees would have been under a duty to initiate abandonment proceedings as soon as they reported, on December 31, 1963, that there was no prospect for independent operations of NH, and that December 31, 1966 is thus an entirely reasonable date for the beginning of the assumed liquidation. Indeed, they insist they are entitled to be fully protected against losses thereafter—a contention we shall discuss below. Our rejection of that contention, see section VII of this opinion, means that a considerable portion of the losses will be borne by the NH estate, and there would be no justification for a double deduction. Beyond that, the Commission had to pick a date for valuation and December 31, 1966 was a reasonable choice. If we were to posit a liquidation beginning only some years hence, we could not simply deduct interim cash losses and depreciation but would have to ask the Commission to revalue the assets and this might yield a higher price."

And again, after referring to "the constitutional right of NH to cease operation and liquidate" because of its large operating losses, the three-Judge Court in its first opinion went on to say unanimously (289 F. Supp. at pp. 440-1, A-359a and 360a):

"We see no reason to question the validity of Justice Holmes' decision in Brooks-Scanlon Co. v. Railroad Commission, 251 U.S. 396, 40 S.Ct. 183, 64 L.Ed. 323, forbidding the State of Louisiana to require a railroad to continue its deficit operation with no hope for profits in the foreseeable future. See also, Mora v. Mejias,

223 F.2d 814 (1 Cir. 1955); Railroad Commission v. Eastern Texas R. R., 264 U.S. 79, 85, 44 S.Ct. 247, 68 L.Ed. 569 (1924); Bullock v. State of Florida ex rel. Railroad Commission, 254 U.S. 513, 41 S.Ct. 193, 65 L.Ed. 380 (1921); cf. Pacific Telephone & Teleg. Co. v. Tax Comm'n, 297 U.S. 403, 413, 56 S.Ct. 522, 80 L.Ed. 760 (1936). We cannot accept the argument that all this was changed by the addition of § 1(18), requiring the Commission's consent to abandonment, to the Interstate Commerce Act by the Transportation Act, 1920, or by the enactment of § 77 of the Bankruptcy Act in 1933. These statutes were designed to assure orderly procedures and to afford methods that might avoid the ultimate solution; they were not intended to override constitutional guarantees, cf. In re Third Avenue Transit Corp., 198 F.2d 703, 707 (2 Cir. 1952), and would not be effective if they had been." [Footnote omitted]

Less than one year later two Judges of the three-Judge Court unaccountably reversed themselves and accepted Penn Central's suggestion of a $15,386,000 reduction in price for an alleged further delay of one year in addition to the six-year period of liquidation, the expenses of which were already fully reflected in the price.

In its May 28, 1969 Opinion, the Reorganization Court said (A-285a):

"It is also inequitable to penalize the New Haven an additional $15,386,000 as the consequence of delaying abandonment in a hypothetical liquidation proceeding, so that the political units and representatives of the public interest could be heard, when, but for the adoption by the Trustees of a course to serve the public interest, abandonment proceedings could and would

have been commenced in late 1963 and liquidation would have been started, certainly by the valuation date of December 31, 1966."

Similarly, the dissenting Judge in the three-Judge Court was vigorous in his rejection of this deduction (Opinion of June 18, 1969, A-435a to 438a) and concluded that the deduction "is without justification and is not based upon substantial evidence."

(b) *Unjustified deduction of a so-called "bulk sale discount" so as to decrease the net liquidation value and price by $6,700,000.* The other expedient which the Commission adopted in order to reduce net liquidation value and the price to be paid by Penn Central was a so-called "bulk sale discount" in the amount of $6,700,000. As was stated by the Reorganization Court (May 28, 1969 Opinion, A-292a) "this deduction is also improper and without support in law or reason."

The Commission sought to justify this newly conceived discount by a discussion under the heading "Limitation on the right to break up the railroad" (334 I.C.C. at pp. 60-3, A-147a to 150a). Accordingly, the primary basis stated for such a discount was the Commission's claimed right to compel a bulk sale of the New Haven assets to a purchaser who would continue the needed rail operations. The Commission then proceeded to measure the discount on such a sale by testimony of a land wholesaler as to the discount he would require in order to purchase the New Haven assets in bulk and sell them at retail. Even the two-Judge majority pointed out (A-417a) two of the fallacies involved, namely, that the Commission did not have the assumed power to compel such a bulk sale of the New Haven for continued railroad use at a reduced price and that the wholesaler on whose testimony the Commission rested was

referring to an assumed wholesale purchaser who would be buying for sale at retail and not for continued railroad use.

Nevertheless, the two-Judge majority proceeded to approve the discount because the Commission had also incidentally said that the "bulk-sale discount merely reflects a market appraisal of the risks that the estate avoids, and the bulk buyer assumes" (334 I.C.C. at p. 61, A-148a).* It is clear that the Commission did not even purport to measure the bulk sale discount by the degree of any alleged risk. It said specifically (334 I.C.C. at p. 61, A-148a) that "we may compel the bulk sale and the bulk sale discount as a condition of an abandonment certificate, and, therefore, as a reduction of the present price"; whereupon it proceeded to deduct an exorbitant discount based on testimony of a land wholesaler which would interpose an unnecessary middleman as a device for reducing net liquidation value below that found by the Commission.**

The dissenting Judge of the three-Judge Court described the bulk sale discount as "an unwarranted duplication of part of the expense already charged to the New Haven" (A-439a). This was clearly so because all the large expenses of a liquidation program through sales at retail over a six-year liquidation period and a $17,000,000 discount to present worth of the liquidation proceeds had

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* As to such risks, the Reorganization Court said (May 28, 1969 Opinion, A-293a): "But the computation in arriving at fair liquidation value has already deducted $8,000,000 for this purpose, in addition to costs and expenses attending the sale of the properties".

** The majority of the three-Judge Court sought to support the bulk sale discount by analogizing it to a premium for underwriting an issue of securities (June 18, 1969 Opinion, A-418a). There is no similarity. In the case of an issue of securities, there is a compulsion to make a successful sale in a short period. In the New Haven situation there is no such compulsion; indeed a six-year period of liquidation was fully provided for.

already been deducted, and there had even been the further $8,000,000 slash of appraised market value to allow for parcels of land which it might be difficult to sell.

The May 28, 1969 Opinion of the Reorganization Court (A-293a) likewise charges the Commission with giving Penn Central a "gift of a double deduction" through this bulk sale discount.

(III) Erroneous refusal to require Penn Central to pay anything for the transfer to it free and clear of any restrictions of that portion ($5,600,000 annually) of New Haven's net income from the Grand Central non-railroad properties which was formerly used to defray New Haven's share of the expenses of the railroad Terminal.

(Question 9)

Among the assets of the New Haven taken over by Penn Central pursuant to the Commission's order was the New Haven's interest (approximately 50%) in hotel and office building properties in the Grand Central area (appraised as a whole at $227,000,000), but the Commission awarded the New Haven no consideration whatsoever for the major portion of this asset. The portion which was taken over by Penn Central without any consideration was the New Haven's share ($5,600,000 per annum) in the net income of these properties which was formerly used to pay Terminal expenses but which at the end of 1968 was conveyed to Penn Central free and clear of any restriction whatsoever as to use. (However, the Commission and the Courts did require Penn Central to give the New Haven $28,400,000 of consideration for the New Haven's share (50%) of the value of the estimated *excess* income of the Grand Central non-railroad properties which had not been used to pay expenses of the Terminal.)

The three-Judge Court refused to disturb the action of the Commission in awarding no consideration for such

$5,600,000 of annual income which has been transferred to Penn Central but the Reorganization Court in its first Opinion stated that, in succeeding to that income, "a valuable interest will have been acquired" by Penn Central (289 F. Supp. at p. 463, A-253a) and left it to the Commission on the remand to find the value.

In the second round the Reorganization Court pointed to the controversy over this asset as support for that Court's conclusion that appeals from both Courts were inevitable and the Court states that, if the New Haven's right to this asset were to be recognized, the record would show a potential worth for this asset of approximately $70,000,000 (Opinion of July 28, 1969, A-314a and 315a).

The principal reason advanced as to why the New Haven should not receive consideration for this asset is that under the old agreement between the New Haven and the New York Central existing prior to the transfer, this portion of the New Haven's share of the net income of the non-operating properties in the Grand Central area was to be used to pay expenses of the Terminal, as was the corresponding share of net income belonging to New York Central. But this agreement was wiped out by its transfer on December 31, 1968 by the New Haven to the other party to the agreement (Penn Central, as successor by merger to Central). The agreement is no longer in existence, and Penn Central now has this income (both the former New York Central's share and the former New Haven's share) free and clear of any restriction against its use in any way Penn Central sees fit. In other words, Central's (now Penn Central's) share as well as the New Haven's former share in such income is by reason of the transfer no longer subject to any restriction of any kind in the hands of Penn Central. Nevertheless, the New Haven has received nothing for such transfer of its $5,600,000 per annum to Penn Central free

of restriction or for such release of the restriction on the Penn Central share.

There is no basis for treating the New Haven's $5,600,000 per annum of net income as being without value on the closing date, with the result that its transfer to Penn Central is not reflected in the purchase price. Other adjustments had to be made in liquidation value to arrive at the purchase price on the closing date and an adjustment should also have been made for the New Haven's valuable interest in this net income. The other adjustments to liquidation value to which we refer are those for New Haven assets not sold to Penn Central and those for accrued real estate taxes which the New Haven remained bound to pay.

(1) Since, under the Purchase Agreement as approved, a substantial amount of New Haven assets were retained by the New Haven Trustees, the New Haven's liquidation value had to be adjusted downward in order to exclude the value of the retained assets (331 I.C.C. at p. 661, A-19a). (2) Since the property was conveyed to Penn Central free and clear of accrued tax liens, the amount of such taxes which had been deducted to arrive at liquidation value had to be restored to the value and the purchase price in order to reflect the contract situation (334 I.C.C. at p. 40, A-127a). (3) Since the New Haven's share of income of the Grand Central non-railroad properties theretofore used to defray Terminal expenses was conveyed to Penn Central free and clear of the restrictive Terminal agreement providing for payment of Terminal expenses and was usable by Penn Central for any purpose on and after the closing date, the 100% discount from the value of this stream of income on account of such former restriction must be restored to the value and the price.

The three-Judge Court bypassed the New Haven's clear right upon the closing date to payment for all of its interest

in the net income of the Grand Central non-railroad properties. It did so by indulging in an irrelevant discussion of the alleged ability of the State of New York to take over operation of the railroad line into the Terminal and obtain free access to the Terminal (A-419a and 420a). Such free access for the State is said to be predicated upon the New Haven's interest in the hotel and office building net income vanishing upon liquidation of the New Haven and therefore being unsalable by the New Haven to the State. But that kind of presentation creates the proverbial straw man.

We have not contended that the New Haven would have to be compensated by the State of New York, as its putative successor in the Terminal railroad operation, for New York's obtaining the right to take over the former New Haven railroad operation into the Terminal. What is involved is the right of the New Haven to obtain compensation from Penn Central for its interest in the Grand Central hotels and office buildings which were jointly constructed and financed by the New Haven and New York Central. In a final decision of the New York Courts in a litigation between the New Haven and New York Central involving one of the Grand Central hotels, it was held that the New Haven and New York Central each had a vested partnership interest in the Grand Central hotels and office buildings (*New York Cent. R.R. Co.* v. *New York, New Haven & Hartford R.R. Co.*, 24 Misc. 2d 414 (Sup. Ct. N.Y. County, 1960), *modified* (in a respect not relevant here), 13 A.D. 2d 309 (1st Dept., 1961), *aff'd without opinion*, 11 N.Y. 2d 1077 (1962)).

To that partnership property belonging to the New Haven the State of New York would have no possible claim if it should succeed to the railroad operation—it could not confiscate the New Haven's interest in those non-railroad properties, or even condemn such non-railroad properties upon

payment of just compensation. Following New Haven's inclusion, the State could acquire that interest only by purchase from Penn Central.

Penn Central has argued that New Haven's partnership share in the non-operating income is irrevocably "dedicated" to payment of Terminal expenses. It is not apparent on what legal theory this so-called "dedication" or pledge might be claimed to survive the cancellation of the agreement said to contain such obligations. The argument seems to be that the claimed survival results from creation of a trust relationship which somehow subjected this stream of New Haven income forever to payment of Terminal expenses. There is no substance to any such trust theory.

No trust theory is needed to explain why, while the basic agreement existed and the New Haven used the Terminal, it was obligated under contract principles to pay its share of the Terminal expenses as provided in the agreement. It is equally clear that no trust theory can support the Penn Central concept that, upon termination of the basic agreement, the New Haven's stream of income from the non-operating properties remains perpetually and irrevocably "dedicated" to the payment of a portion of Terminal expenses.

It is hornbook law that in order to create a trust "there must be either an explicit declaration of trust, or circumstances which show beyond reasonable doubt that a trust was intended to be created." (*Title Guarantee & Trust Co.* v. *Haven,* 214 N.Y. 468, 481 (1915)). Neither such an explicit declaration nor any indication of such an intention exist here, let alone an intention shown "beyond reasonable doubt."

The basic agreement contained nothing which intimates that the New Haven's partnership interest in the non-

railroad properties was to be subject to a trust to pay Terminal expenses which would survive the termination of the agreement. Who are the trustee and the beneficiary of that trust? Certainly they cannot both be Penn Central as a trustee for itself. Or is this "trust" to have no trustee or beneficiary and be operated by a disembodied spirit which, after termination of the basic agreement, will somehow without human intervention funnel net income from the non-operating properties directly to payment of Terminal expenses for the benefit of "whom it may concern"?

The New Haven has been deprived by the Commission and the Courts below of up to $70,000,000 in capitalized value because of the failure to require Penn Central to pay any compensation to the New Haven for the transfer to Penn Central, free and clear of restrictions, of the New Haven's partnership share in the hotel and office building net income ($5,600,000 per annum) formerly used to defray Terminal expenses.

(IV) Erroneous limitation on Penn Central's sharing of New Haven losses in period after merger of Penn and Central.

(Questions 10 and 11)

The Commission in the Second Supplemental Report (331 I.C.C. at pp. 714-20, A-72a to A-78a) approved a formula for the "sharing" of New Haven losses by Penn Central from the date of the Penn Central merger to the date of New Haven's inclusion. The formula is inadequate in two substantial respects. First, the Commission placed an arbitrary limit of $5,500,000 a year (prorated to $5,000,000 for 11 months) on the amount of Penn Central's "share" of the New Haven loss; and second, it arbitrarily omitted from the formula substantial items of loss which should have been included. For the 11 months, the formula loss was about $7,500,000 and the total loss, including items arbitrarily omitted, was in excess of $10,000,000.

At the time the limit of $5,500,000 a year was fixed by the Commission (Second Supplemental Report, 331 I.C.C. at p. 718, A-76a), it was somewhat in excess of the amount, $5,400,000, which the Commission estimated would be the formula loss of the New Haven for the first year following the Penn Central merger. The Commission based that finding on the New Haven's figures for 1967 (A-75a to 76a), which were the latest figures then available. Accordingly, the limit was not originally fixed with any idea of having it result in a "sharing" of the formula loss between New Haven and Penn Central, but the Commission intended to have Penn Central take up the entire formula loss for the initial year following the Penn Central merger.

All the subsequent discussion by the Commission and the Courts relating to Penn Central not taking up all the formula losses of the New Haven for the period involved was caused by the accident that the formula loss figure for the first year prior to inclusion increased, by the time the Courts dealt with the matter and the Commission dealt with the matter on remand, from the original $5,400,000 per annum based on 1967 figures to $8,200,000 per annum based on 1968 figures (334 I.C.C. at p. 73, A-160a). Notwithstanding the increase, the Commission left the limit as originally fixed by it, although it no longer covered the indicated annual New Haven loss, with a view to not increasing the payment to be made by Penn Central over that originally fixed by the Commission.

The inclusion of the New Haven was delayed for the convenience and benefit of Penn Central as the Reorganization Court noted (289 F. Supp. at p. 461, A-248a). Accordingly, the July 1968 Opinion of the dissenting Judge stated (289 F. Supp. at p. 449, A-378a):

> "Had that which should have been done, been done at the time of the merger, New Haven then would have

become a unit of Penn Central, with the latter necessarily absorbing operating losses from the date of the merger; to require Penn Central to do so now imposes no unjust or onerous terms upon it. Penn Central, as the beneficiary of the merger, would be assuming a burden which was part of a single transaction—this, entirely apart from the creditors' claim that, constitutionally, they cannot be forced to bear the increased losses entailed by the continued operation of the New Haven pending inclusion."

Referring to such view of the dissenting Judge, the Reorganization Court said in its 1968 Opinion (289 F. Supp. at p. 461, A-248a) that "the cogency of what Judge Weinfeld said is apparent."

In the dissenting Judge's June 18, 1969 Opinion (A-442a), he reiterated this view, saying, "Consistent with my view previously expressed, the entire interim operating losses should be borne by Penn Central."

The majority July 1968 Opinion (289 F. Supp. at p. 443, A-365a) did not find the choice between the contending views to be "easy", but it accepted the Commission's arbitrary limitation on Penn Central's loss sharing.

In addition, there is no basis for the arbitrary inclusion in the formula of some losses of the New Haven and the exclusion of others. Among those arbitrarily and wrongfully excluded are rent for leased roads—$734,000, and interest paid during bankruptcy (none of it on defaulted securities)—$1,936,000, based on 1968 figures.

There is no legal basis or standard put forward, nor could there be, for the limitation imposed or for the exclusion of some items of loss while including others. Either there was no equitable obligation on Penn Central to pay

any of the New Haven loss during the period from the Penn Central merger to the date of its acquisition of the New Haven assets or there was an obligation to pay the entire loss. Obviously, as was stated by the dissenting Judge of the three-Judge Court, there is an equitable obligation on the Penn Central to pay the entire loss. That there was such an obligation is clearly indicated by the fact that the Commission and *all* the Judges in the case, without exception, felt that Penn Central should pay some losses of the New Haven during this period without any valid reason being advanced as to why it should be less than all.

We submit that the limit on the loss sharing to $5,000,000 for the 11-month period and the exclusion of items of real loss were erroneous as a matter of law, were without substantial support in the record and were arbitrary and capricious.

(V) Erroneous ruling as to valuation of Oak Point and Harlem River Yards.

(Question 12)

In its July 1968 decision, the three-Judge Court ruled (289 F. Supp. at pp. 433-4, A-344a and 345a) that no adequate explanation was made in the Second Supplemental Report why the Commission had rejected the realty expert McCann's higher appraisal ($22,650,000) and accepted instead his lower appraisal ($18,100,000) of the value of the Oak Point and Harlem River Yards.

After the remand, Mr. McCann testified in the fall of 1968 (at the 1967 hearings, Mr. McCann had not testified but his two appraisals were put in evidence by the head

of the New Haven's real estate department). It then developed that his lower ($18,100,000) appraisal assumed that upon the New Haven's liquidation the industrial users of these Yards would be left without railroad service while the adjusted higher appraisal ($22,540,000) assumed continuance of railroad service. It further developed that, when Mr. McCann made his lower appraisal, Mr. McCann did not know that between the Oak Point Yard and the New York Central's adjacent Port Morris Yard there was an existing railroad connection (Tr. p. 28881) through which railroad service to the Yards could be continued notwithstanding a liquidation of the New Haven.

In its June 1969 decision (A-423a), the majority of the three-Judge Court nevertheless accepted the Commission's conclusion that, upon the New Haven's liquidation, there would be no railroad service to these Yards. On the other hand, the dissenting Judge of the three-Judge Court and the Reorganization Court were emphatic in ruling (Reorganization Court May 28, 1969 Opinion, A-295a to A-297a; minority June 18, 1969 Opinion, A-442a and 443a) that the clarifying testimony introduced pursuant to the remand decision showed that the Commission's original $18,100,000 valuation had been made on an erroneous basis and that the Commission's adherence in the Fourth Supplemental Report to the original $18,100,000 valuation was without substantial support in the evidence and unlawfully deprived the New Haven of $4,440,000 of value.

(VI) Excessive present worth discount deducted from the proceeds of the assumed liquidation of the New Haven.

(Question 13)

The Commission in its Second Supplemental Report deducted $17,563,000 as a discount to present worth of the liquidation proceeds to be received over a six-year period of liquidation. Bondholder interests have contended that the record demonstrates that the discount of gross receipts adopted by the Commission was excessive by over $2,000,000.

The Reorganization Court upheld such contention of the bondholders and in its July 28, 1969 order (A-318a) directed that the "sum of $2,415,899 should be added to liquidation value inasmuch as it was improperly deducted in applying the discount to present value found by the Commission".

In the Memorandum of the majority of the three-Judge Court dated September 11, 1969 (accompanying its Decree of the same date), the majority (A-445a) refused to pass on the merits of this deduction on the ground that the precise amount of the deduction was calculated in a letter from bondholder interests dated June 17, 1969, received by both Courts after they had rendered their respective decisions in May and June. However, the decrees were then still to be formulated and such calculation was but one of several which had been made by bondholder interests subsequent to the Second Supplemental Report. Bondholder interests contended in these proceedings, long before these Court decisions, that the discount of gross receipts to present worth was substantially excessive.

We submit that it was error for the majority of the three-Judge Court to refuse to pass on the merits of this issue.* The majority September 11, 1969 Memorandum said on this subject (A-445a):

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* Incidentally, the September 11, 1969 Memorandum of the majority of the three-Judge Court refers (A-445a) to the bondholders' proposed reduction of $2,695,899 in the discount to present

"We have not passed on the merits of this contention since we do not consider it to be appropriately before us on settlement of the decree. The difference in the treatment of this item by the two courts will be another matter for ultimate resolution by the Supreme Court."

(VII) The formula invented by the Reorganization Court and adopted by the three-Judge Court to guarantee the $87.50 value per share assigned by the Commission to the Penn Central stock received by the New Haven contains provisions which would interfere with the achievement of a basic intention of the reorganization plan.

(Question 14)

As the three-Judge Court expressly recognized, it was the intention of the plan of reorganization of the New Haven that the Penn Central stock received by the New Haven as the major part of the consideration would be held pending the *long-term* realization by Penn Central of the savings and other benefits anticipated from the Penn Central merger.* Thus, the June 18, 1969 majority opinion of the three-Judge Court stated (A-430a):

"It must have been expected from the outset that a large portion of the purchase price would consist of PC stock and that this would not be immediately sold but rather would be held by the reorganized NH as a

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worth while the amount deducted by the Reorganization Court in its order is $2,415,899 (A-318a). The difference of $280,000 arises because of the issue as to whether the lower or higher appraisal of the Oak Point and Harlem River Yards is to be accepted. The Reorganization Court's lower reduction assumed acceptance of its higher valuation of those Yards, whereas the higher reduction mentioned by the three-Judge Court assumed acceptance of the lower valuation of the Yards.

* The Commission estimated the savings resulting from the Penn Central merger to be realized after about eight years at over $80,000,000 per annum (327 I.C.C. at p. 501).

major long-term participant in what was expected to be a great and successful railroad system."

The Commission assigned a *short-term* value of $87.50 per share to the Penn Central stock but the stock has not as yet sold at that price. Therefore, the Reorganization Court invented a formula (adopted in substance by the majority of the three-Judge Court) which was intended to guarantee the realization of at least that price over the 10-year period following the Penn Central merger (A-300a and 301a).

The basic provision of that formula is that Penn Central would pay the New Haven on February 1, 1978 the excess, if any, of $87.50 per share over the mean price of the Penn Central stock for the 30 business days next preceding that date. However, because of the two "outs" in the formula which are referred to below, the formula not only does not carry out its purpose but it interferes with achievement of the above-stated intention of the reorganization plan.

The two "outs" mentioned above are:

One. Penn Central has no obligation to make any payment if the market value of the shares reaches and maintains $87.50 on the Exchange for only five consecutive days at any time before February 1, 1978; and

Two. Penn Central is also relieved from any further obligation in respect of specified blocks of the shares by designating, five days in advance, any business day prior to February 1, 1978 and paying to the New Haven the deficiency, if any, between the quoted sale price of the shares on that day and $87.50 per share.

We submit that these two "outs" not only make the formula insubstantial but their operation would invite the reorganized New Haven to sell Penn Central shares in advance of the termination of the formula period.

The "outs" make the formula insubstantial because they could relieve Penn Central at an early date from its obligation on the basis of a few transactions on the Exchange regardless of the number of shares dealt in or the depth of the market or whether a large block of Penn Central stock could be sold at the price indicated.

Moreover, operation of either of the two "outs" would interfere with the intention of the reorganization plan because it would induce the directors of the reorganized New Haven prematurely to sell Penn Central stock. Whichever one of the "outs" was involved, its operation would put pressure on the directors to sell Penn Central shares at an early date in order to avoid criticism if the price of the stock should subsequently decline.

More specifically, if the Penn Central obligation expired because the $87.50 price was attained for five days well before the end of the 10-year period, the directors would in all probability sell shares promptly in that market because they no longer had the protection of the Penn Central obligation. Similarly, if Penn Central were to terminate its obligation in respect of large blocks of shares by paying a deficiency based on transactions of a single day, the directors could be expected to sell those shares at a price which, including the deficiency payment, would realize $87.50 or near that figure in order to protect themselves against a possible subsequent decline in the market price.

On the other hand, if New Haven directors have the unconditional assurance of eventually obtaining at least $87.50 per share at the end of the 10-year period, they would have the incentive to hold the stock intact, as is the intention of the reorganization plan, in order that the New Haven have the opportunity to realize substantially more than $87.50 per share.

Clearly, operation of either of the two "outs" embodied in the guarantee formula would interfere with the intention of the reorganization plan that the Penn Central stock be held for the formula period, rather than being sold in the meantime, so that the New Haven might be a long-term participant in the savings and benefits expected to result from the Penn Central merger.

Conclusion

This Court has jurisdiction of this appeal and substantial questions are presented, particularly in view of the conflict between the Judges below.

We submit that this Court should note probable jurisdiction.

Respectfully submitted,

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December 5, 1969